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TAGS: [EFIN](#) [ECON](#) [EINV](#) [RS](#)
SUBJECT: TREASURY DEPUTY SECRETARY KIMMITT'S JUNE 21
MEETING WITH CENTRAL BANK CHAIRMAN IGNATIEV

Classified By: Ambassador William J. Burns, Reasons 1.4 (b/d).

11. (C) Summary. In a June 21 meeting with Deputy Treasury Secretary Robert M. Kimmitt, Russian Central Bank (CBR)

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Chairman Sergey Ignatiev provided a generally positive overview of the Russian economy. On the subject of investing Russia's oil and gas tax revenue, Ignatiev observed that the CBR would play a consultative role regarding the Finance Ministry's plans to invest the resources of the Stabilization Fund, which will be reorganized into the Reserve Fund and the National Welfare Fund in early 2008. He emphasized that the CBR's role was one of establishing macroeconomic conditions needed to sustain an attractive investment climate. He said that the CBR had helped facilitate improvements in such indicators such as reduced unemployment, rising wages, declining inflation, and a strengthening ruble. He also observed, however, that although Russia's banking sector was one of the fastest growing and, in terms of foreign investment and ownership, was one of the least restricted segments of the economy, it suffered from a perception of vulnerability and instability. Ignatiev explained that the prevalence of such views has been the principal obstacle regarding the issue of foreign bank branching in Russia. Kimmitt thanked Ignatiev for the CBR's participation in the transfer of funds to the North Korean Foreign Trade Bank's account with the Far Eastern Commercial Bank in Khabarovsk. End Summary.

12. (C) GOR Investments. Treasury Deputy Secretary Kimmitt met with Central Bank (CBR) Chairman Ignatiev to thank the CBR for its role in the transfer of North Korean funds from Banco Delta Asia to the Far Eastern Commercial Bank in Khabarovsk. They also discussed the CBR's role in managing the GOR's windfall oil profits in the Stabilization Fund--which will be reorganized as a Reserve Fund and National Welfare Fund in early 2008--as well as its responsibilities in working to establish macroeconomic stability needed to attract foreign investment. Ignatiev explained that the Finance Ministry is the primary decision maker for investing Stabilization Fund resources but added that the CBR does play, and will continue to play, a consultative role even after the Stabilization Fund's reorganization. Ignatiev echoed other officials' views that neither the GOR in general nor the Finance Ministry in particular had plans to use the Stabilization Fund for direct investment purposes or to establish a controlling stake in

any foreign corporation, state-owned or private.

¶3. (C) Investment Climate. Chairman Ignatiev said that the CBR would have very little involvement in the content and direction of the Strategic Sectors Law. He outlined that the CBR was charged with facilitating macroeconomic conditions that would produce an attractive investment climate. Focused on lowering inflation, the CBR has helped bring down unemployment to its lowest level since 1992, just 7 percent by International Labor Organization measures. Full ruble convertibility and capital account liberalization in July 2006 pushed net private capital inflows to nearly USD 42 billion by the end of the year, and net private capital inflows for 5m07 have already reached USD 60 billion. Maintaining relatively low interest rates has fueled growth in manufacturing and industrial production. Ignatiev observed that, although the economy was growing at "a good rate" and that the country was "on track" to meet its inflation target for the year, the banking sector was showing some signs of overextension.

¶4. (C) Banking Sector. Ignatiev described the banking sector as one of the most profitable and least restricted segments of the Russian economy. Profit ratios exceed 20 percent for most of the sector, and the law does not impose a limit on foreign ownership. He nevertheless expressed concern that the growing volume of non-performing loans might shake depositors' confidence in the sector as a whole. Banking assets grew nearly 40 percent during 2006, with consumer lending taking the lion's share. In an effort to address questionable lending practices and to educate borrowers, the CBR would soon begin requiring that lenders fully disclose their effective interest rates to borrowers, inclusive of fees, commissions and other expenses. Ignatiev hastened to add, however, that the CBR currently sees no signs the banking sector is overheating.

¶5. (C) Foreign Branching. In response to a question about foreign branching in Russia, Ignatiev explained that although the Russian banking sector was open to foreign investment, it had not yet become competitive against foreign branching. He summarized the Russian banking community's fear that branching by foreign banks would lead to the collapse of Russian banks. Ignatiev recounted that the deposit insurance program was still in its infancy and had its first test immediately following implementation. In 2004, a money laundering allegation against a bank provoked a run on the bank, which Russian bankers do not want to see repeated. He expressed confidence that with time, as deposits continue to rise in line with positive sentiment about the deposit insurance program, the banking sector will be able to support foreign branching.

¶6. (U) Deputy Secretary Kimmitt has cleared this message.
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